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In the Supreme Court of the United States

OCTOBER TERM, 1941

No. 923

PHILLIPS PIPE LINE COMPANY, PETITIONER

v.

THE UNITED STATES

ON PETITION FOR A WRIT OF CERTIORARI TO THE COURT
OF CLAIMS

BRIEF FOR THE UNITED STATES IN OPPOSITION

OPINION BELOW

The opinion of the Court of Claims (R. 33-38) is reported in 40 F. Supp. 981.

JURISDICTION

The judgment of the Court of Claims was entered October 6, 1941 (R. 38). The petition for a writ of certiorari was filed February 5, 1942, the time for filing having been extended by an order of this Court entered November 14, 1941 (R. 867). Jurisdiction of the Court is invoked under section

3 (b) of the Act of February 13, 1925, as amended by the Act of May 22, 1939.

QUESTION PRESENTED

Whether natural gasoline is crude petroleum or a liquid product thereof within the meaning of section 731 (a) of the Revenue Act of 1932.

STATUTE INVOLVED

Revenue Act of 1932, c. 209, 47 Stat. 169:

SEC. 731. TAX ON TRANSPORTATION OF OIL BY PIPE LINE.

(a) There is hereby imposed upon all transportation of crude petroleum and liquid products thereof by pipe line * * *.

(1) A tax equivalent to 4 per centum of the amount paid on or after the fifteenth day after the date of the enactment of this Act for such transportation. * * *

STATEMENT

The special findings of fact made by the Court of Claims (R. 24-33) may be summarized as follows:

During the years 1932 through 1936 petitioner corporation was engaged in the business of transporting by pipe line refinery gasoline, natural gasoline, and butane (R. 24). The three products were transported by petitioner separately and were kept in separate tanks at petitioner's pipe-line terminals (R. 24-25). For the period June 20, 1932, to March 31, 1936, inclusive, petitioner paid \$264,-

784.38 taxes in respect of its transportation of natural gasoline and butane (the amount paid in respect of butane being \$29,407.21) (R. 25).

All of this natural gasoline and butane was produced in the Panhandle Field of Texas. The field's major importance is as a gas reserve, although many wells produce gas from an upper structure and oil and gas from a lower. All structures produce oil at sea level, and all appear to be intercommunicative. In the Panhandle area two types of wells are recognized: one that produces only gas, and the other which produces both gas and oil. (R. 26.)

There are three general types of natural gas: (1) gas well gas, coming from a straight gas well, (2) gas cap gas, coming from formations above oil strata, and (3) solution gas, which comes in solution with oil from a well (R. 27). The first two types are carried directly by a pipe line to a natural gasoline plant (R. 27). Solution gas is carried with its solvent oil from the well by pipe to a separator, where the gas rises and enters a gas pipe line to the natural gasoline plant (R. 28).

From the well or from the separator the oil is carried by pipe line to a stock tank, where it is allowed to stand for several days for settling out of basic sediment, water, and sand. The remaining liquid, known as "merchantable" or "pipe-line"

oil, is then piped to permanent storage tanks or into commerce. (R. 28.)¹

At the natural gasoline plant natural gasoline is extracted from natural gas by means of charcoal absorption, compression, or oil absorption (R. 28-29). The natural gasoline is then transported by pipe line and marketed (R. 28). Natural gasoline is highly volatile (R. 29). From 1932 to 1936 it was not satisfactory for use alone as a motor fuel; it required stabilization and blending with refinery gasoline,² and the total American production of natural gasoline was almost entirely so used during the years in question (R. 29).

One of the hydrocarbon components of natural gas is butane. In the extraction of natural gasoline from natural gas, butane is segregated as a liquid and is thereafter stored, shipped, and sold as a liquid. Butane is a gas at temperatures above 30° F. unless kept under pressure. It is classified as a "liquefied petroleum gas". (R. 29.)

Commercial operators and dealers in oil and gas generally understand the terms "crude", "crude oil", "crude petroleum", and "crude petroleum oil" as designating "merchantable" or "pipe-line" oil. The terms "crude" and "crude oil" are the terms generally used in daily trade parlance, while

¹ Natural gas is sometimes obtained from stock or storage tanks, where it may escape from the oil; from the tank it is piped to a natural gasoline plant (R. 27).

² These operations are performed at pipe-line terminals or at oil refineries (R. 28).

the terms "petroleum" and "crude petroleum" are used in technical writings. Operators and dealers regard natural gasoline as a product of natural gas and not as a product of crude petroleum. Those engaged in the oil and gas industry or industries treat oil and gas as separate and distinct commodities, with different pricing and handling. Leases and contracts for the production of and payment of royalties on oil and gas provide separately for the two commodities. (R. 29-30.)

Scientists and engineers, however, employ "crude petroleum" as a broader definition, denoting the entire hydrocarbon content of a reservoir,³ natural gas included; estimates of oil and gas in place are reported as "petroleum reserves", and comprise all forms that may be found, in gaseous, liquid, or solid state. This view is based on the scientific conception of natural gas, natural gasoline, refinery gasoline, kerosene, fuel and lubricating oils, paraffin wax, etc. as groupings of certain related compounds (of carbon and hydrogen), with each grouping containing the same compounds as the other groupings but in varying proportions. The most important of these compounds (in the paraffin series of hydrocarbons) are methane, ethane, propane, butane, pentane, hexane, heptane,

³ The total content of the reservoir is termed "reservoir fluid" (R. 31).

octane, nonane, and decane.⁴ Natural gasoline, while resembling refinery gasoline, contains a larger percentage of the lighter hydrocarbons, butane, pentane, and hexane, than refinery gasoline.⁵ There is no definite chemical dividing line between natural gas, natural gasoline, refinery gasoline,⁶ and crude oil. (R. 31.)

The physical state of the hydrocarbons and their recognized groupings may be changed readily by variations of temperature and pressure: hydrocarbon gases may be liquefied by cooling and compression, and liquids may be transformed into a gaseous state (R. 31-32). "Crude oil" is defined by scientists and engineers as the liquid portion of petroleum in unrefined form (R. 32). "Natural gas" is defined as the naturally occurring mixture of gaseous constituents of petroleum (R. 33). "Natural gasoline" is defined as a series of hydrocarbons which are the lighter fractions of crude oil;⁷ it is a liquid at normal temperature and pres-

⁴ The groupings also contain traces of heavier hydrocarbons (R. 31). The basic formula for all of the compounds in this hydrocarbon series is C_nH_{2n+2} . See 5 Encyclopedia Britannica (14th ed.) 365-366.

⁵ See Pet. Ex. 16, R. 720A.

⁶ Refinery gasoline manufactured by "cracking" processes is an exception (R. 31).

⁷ These same hydrocarbons exist as a vapor in natural gas, from which natural gasoline is extracted, conversely as the lightest hydrocarbons (methane, ethane—gases under normal conditions) exist to some extent dissolved in crude oil and in refinery gasoline (R. 28; 720A).

sure, and is stored and shipped in that state (R. 33).

In June 1936 petitioner filed a claim for refund of the taxes paid by it with respect to the transportation of natural gasoline and butane (R. 9-11, 26). In December 1936 the Commissioner of Internal Revenue rejected the claim (R. 23, 26). Petitioner on December 14, 1938, filed in the Court of Claims a petition for refund of taxes (R. 1-7). After hearing before a commissioner and argument (R. 24), the court at the conclusion of its special findings of fact (summarized pages 2-7, *supra*), found that natural gasoline is a liquid product of crude petroleum (R. 33). Accordingly, it concluded that petitioner's taxes had been rightly paid (R. 33), and gave judgment dismissing the petition on October 6, 1941 (R. 38).

ARGUMENT

Congress in section 731 (a) of the Revenue Act of 1932 specified for taxation the transportation by pipe line of "crude petroleum and liquid products thereof". Section 500 (d) and section 500 (e) of the Revenue Acts of 1917 and 1918, respectively, had laid a tax on the carriage of "oil by pipe line".⁸ When the tax was sought to be revived in the Reve-

⁸ C. 63, 40 Stat. 315; c. 18, 40 Stat. 1102. These tax provisions were subsequently repealed. Sec. 500 of the Revenue Act of 1918, c. 18, 40 Stat. 1101; sec. 1400 (a) of the Revenue Act of 1921, c. 136, 42 Stat. 320.

nue Bill of 1932, it first appeared as a committee amendment in the House of Representatives, and the words of designation, "oil by pipe line", were adopted without change. 75 Cong. Rec. 7225-7226, 7229. The Senate Committee on Finance changed "oil" to "crude petroleum and liquid products thereof", with the explanation that: "This will make transportation of gasoline as well as crude oil taxable." S. Rep. No. 665, 72d Cong., 1st sess., p. 47.⁹ The intention of Congress regarding the scope of *gasoline* may well be inferred from the definition given in section 617 (c) of the Revenue Act of 1932 (manufacturers' excise provisions):

(2) the term "gasoline" means gasoline, benzol, and any other liquid the chief use of which is as a fuel for the propulsion of motor vehicles, motor boats, or aeroplanes.

There is thus apparent a plain legislative purpose to cover by the pipe-line transportation tax liquids commonly sold and used as *gasoline*. The exemption of natural gasoline, chemically similar to refinery gasoline and used for the same purposes (being blended with refinery gasoline before marketing), ought not be implied in the absence of clear evidence that Congress intended to except it from the petroleum liquids designated in the tax statute.

⁹ The change was accepted in the conference report. H. Rep. No. 1492, 72d Cong., 1st sess., pp. 1, 26. The new language may have been unnecessary in view of Article 91 of Treasury Regulations 49 (1919) which defined "oil" under the earlier transportation tax provisions as "crude petroleum and such of its products as may be transported by pipe line."

Petitioner challenges the Court of Claims finding that natural gasoline is a liquid product of crude petroleum on the narrow ground that "crude petroleum" signifies only "merchantable" or "pipe-line" oil, which remains after the settling in stock tanks of an oil well's fluid output; petitioner then argues that since natural gasoline is produced from natural gas rather than from merchantable oil it is not covered by section 731 (a). This interpretation of "crude petroleum" is grounded ultimately on a specialized trade usage of the term (see Pet. 13-18), and in consequence should not govern in construing the tax statute. Cf. *McCaughn v. Hershey Chocolate Co.*, 283 U. S. 488, brief for respondents, pp. 9-10.

The interpretation which the Court of Claims accorded to "crude petroleum" is that held by scientists and engineers, being dictated by scientific considerations in the chemistry of petroleum. See Statement, *supra*, pp. 5-6. Since it is in harmony with the sense of the taxing statute, the decision of the court below preferring this interpretation to that contended for by petitioner is sound.

The Court of Claims construction in this case of section 731 (a) with respect to natural gasoline is that which has been employed consistently by the Treasury in administration of the tax. In S. T. 564, XI-2 Cum. Bull. 531 (1932), the Bureau of Internal Revenue ruled:

"Natural or casinghead gasoline is a liquid product of crude petroleum, within the

meaning of section 731 of the Revenue Act of 1932, and the transportation thereof by pipe line is subject to the tax imposed by that section of the law. * * *

Likewise the federal courts which have previously considered the problem of the present case have held the transportation of natural gasoline taxable under section 731. *Standard Oil Co. of Cal. v. United States*, 39 F. Supp. 180 (N. D. Cal.); *General Petroleum Corp. v. United States*, 24 F. Supp. 285 (S. D. Cal.).

Petitioner urges that the decision below is in effect a holding that the transportation of natural gas by pipe line is taxable under section 731 (a) of the Revenue Act of 1932, and that such an important consequence of the Court of Claims position calls for review by this Court (Pet. 18-19). But it is apparent that the decision of the court entails no such result. As petitioner states (Pet. 18; see R. 616), the Treasury has never sought to collect a tax under section 731 on the transportation of natural gas. It is apparent from the background, terms, and legislative history of the statute that the object of taxation is the transportation of petroleum liquids (see pages 7-8, *supra*); natural gas is excluded. Cf. 75 Cong. Rec. 7226.¹⁰ Accordingly, the objection of petitioner is not well taken.

¹⁰ Representative Crisp, who introduced the Revenue Bill of 1932, there stated in answer to a question that the pipeline tax would not cover natural gas.

Butane, as the Court of Claims found (R. 29), is a constituent compound of natural gas; after segregation from natural gas it is stored, shipped, and sold as a liquid. Contrary to the contention of petitioner (Pet. 25), the decision below with respect to butane is supported by findings (R. 24, 25, 26, 29) in conjunction with the same reasoning which the court employed to hold taxable petitioner's transportation of natural gasoline; the absence of an ultimate finding, *in haec verba* that butane is a liquid product of crude petroleum, is immaterial.

CONCLUSION

The decision of the Court of Claims is sound, and no conflict of decisions is presented. It is therefore respectfully submitted that the petition should be denied.

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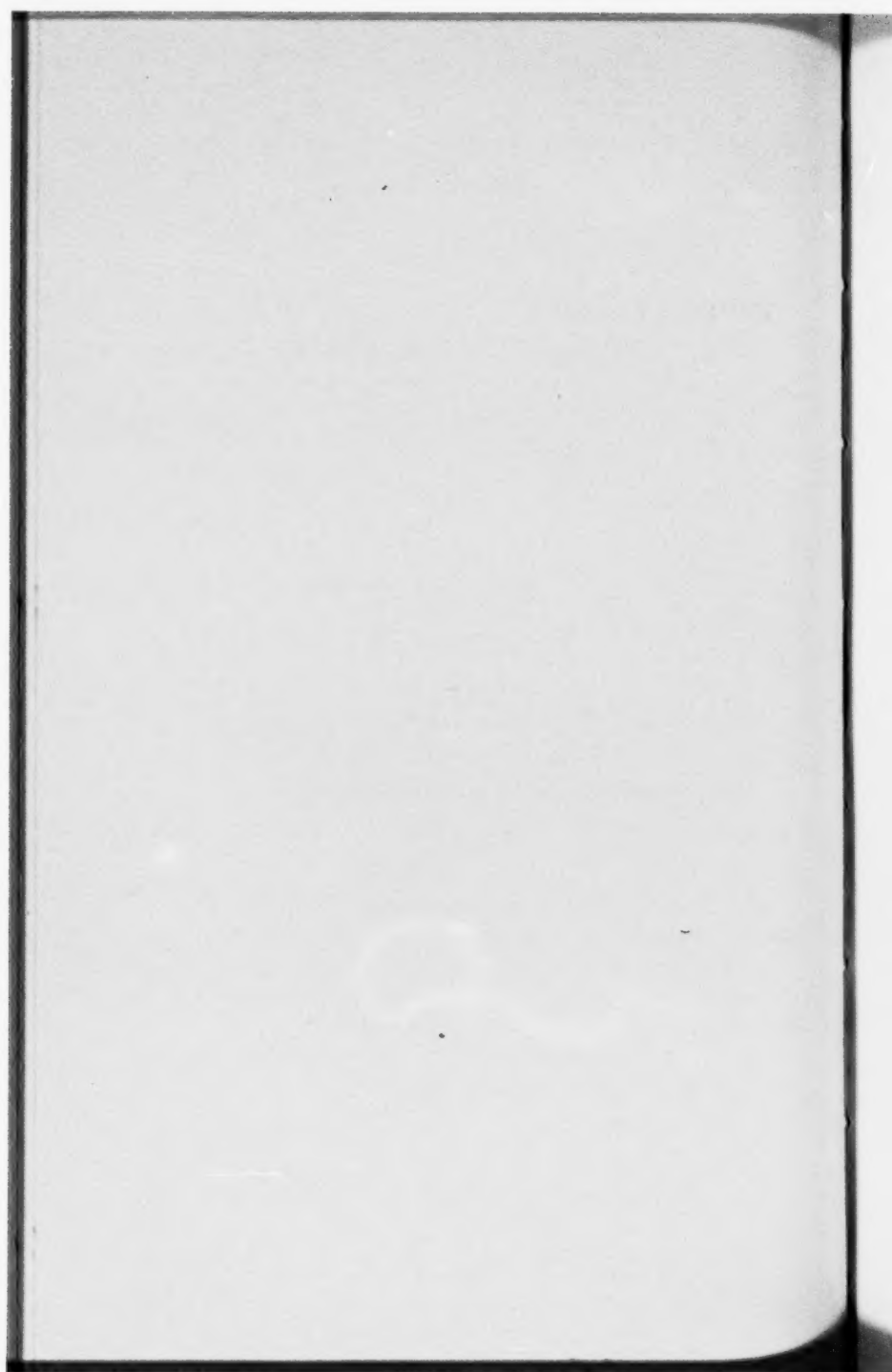
THE PHILLIPS PIPE LINE COMPANY, a Corporation,
Petitioner,

v.

THE UNITED STATES.

—
PETITIONER'S REPLY BRIEF.
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PETITIONER'S REPLY BRIEF.

The Brief in Opposition states that the lower Court's definition of "crude petroleum" should be adopted. See *Brief in Opposition*, at p. 9. Then the Brief proceeds on the very next page to argue that natural gas is not "crude petroleum". See *Brief in Opposition*, at p. 10.

The lower Court's definition of "crude petroleum" appears in its *Finding* No. 22 (R. 32). It is:

" 'Crude petroleum' is a broader term than 'crude oil' and includes the total hydrocarbon substances in the reservoir. *Natural gas, crude oil, asphalt, paraffin wax are all parts of crude petroleum.*"